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BILL ANALYSIS

BILL NUMBER: House Bill No. 6299 (As Introduced)
TOPIC: Trust Powers of Banks
SPONSOR: Representative David Law
COMMITTEE: House Committee on Banking and Financial Services
Analysis Done: September 19, 2006

POSITION

The Office of Financial and Insurance Services supports this legislation.

PROBLEM/BACKGROUND

One of the by-products of the integration of the financial services industry is a narrowing of the investments available for trust account portfolios because of current restrictions on transactions among affiliates. Additionally, current law does not prescribe a definitive mechanism for the assessment of fees for trust services.

DESCRIPTION OF BILL

The Banking Code of 1999 (Code), 1999 PA 276, currently provides that a bank or state foreign bank branch acting as a fiduciary may charge a reasonable fee for its services. The bill would create a rebuttable presumption that a fee is reasonable if both of the following requirements are met:

1. The fee or its method of computation is specified in a fee schedule or agreement in effect at the time the service is provided.
2. The person or persons entitled to notice regarding the trust receive reasonable notice of the fee schedule or agreement before the fee is charged.

The bill also would expand a bank's ability to invest trust assets in transactions with the bank or its affiliates if the document governing the trust doesn't prohibit such transactions. Current law allows for investment of trust assets in same-bank-managed mutual funds; but it permits most other same-bank or affiliate transactions only when

specifically authorized by the trust instrument, a court order or with the consent of all the interested parties of the trust. For large, long-lived trusts with widely dispersed beneficiaries, the latter option can be very cumbersome.

The bill would simplify this process by allowing a bank to use trust assets to purchase products, securities, or services from itself or its affiliates either with the written consent of the grantor of a revocable trust or, for irrevocable trusts or trusts whose grantors are deceased or incapacitated, if the bank has provided at least 45 days advance notice to persons entitled to trust accountings. The purchase price in such a transaction must be reasonable, and the bill does not relieve a trustee of the fiduciary responsibility to meet the "prudent investor" standard. A bank may not proceed to engage in the proposed affiliate transaction for a period of 60 days from receipt of an objection from an interested party if the objection isn't resolved or withdrawn.

The bill also clarifies that a bank or its affiliate engaging in such a transaction may receive compensation for a purchase of a product, service or security under the amendment.

SUMMARY OF ARGUMENTS

Pro

While the current section 4401(2)(e) of the Code [amended to become subsection (3)(e) in this bill] allows a bank with trust powers to receive a reasonable fee for its services, the bill establishes a standard for what is "reasonable." The proposed amendment acknowledges both that it is appropriate for a bank to have and use schedules for assessing fees on trusts and that it is also important for the interested parties of the trust to be aware of fees that may be imposed. Under the proposed amendment, a condition of a fee being determined "reasonable" is that those who are entitled to trust information under the Estates and Protected Individuals Code would receive notice of a bank's fee schedule in advance of imposition of trust fees.

Many current trust agreements allow for the trust administrator to invest trust assets in bank products or purchase securities through the bank or an affiliated broker-dealer, but such explicit authorization is rare in older trusts. A trust administrator that seeks to have an older trust agreement amended to allow the bank's products to be available for investment by the trust often finds very difficult and burdensome the sheer number of interested parties whose consent must be obtained, if the trust grantor is deceased. Alternatively, it is costly to seek judicial authority to make such an amendment to the trust agreement. The bill seeks to balance administrator and beneficiary interests in establishing an alternative means of amending trust agreements to allow the option of trust transactions with the bank or its affiliates and also provide notice to interested parties and an opportunity to object to a change in the investment authority under the trust agreement.

The bill's proponents attempt to balance the interests of trust administrators in easing requirements for approval of investment in bank and affiliate products and services with protection of trust interested parties by requiring advance notice and delaying implementation of changes if interested parties object. The proposed amendment allowing trust administrators to purchase own-bank or affiliate products and services would require either grantor consent or 45 days' advance notice to any person entitled to receive trust accountings. The 60-day delay if an interested party objects to implementing such a change in a trust agreement would provide an opportunity for the trust administrator and the objector to discuss and resolve their differences.

Con

Fiduciaries have traditionally been held to a high standard that has minimized opportunities for self-interest or even the appearance of self-interest to affect decisions regarding the management of trusts. In the past, this has meant that the trust administrator was prohibited (unless specifically authorized by the trust agreement or by the active consent of all the interested parties or by a court) from engaging in trust asset transactions with the commercial side of the bank.

It should be noted that, traditionally, the investment products trusts held were not available from banks. For much of the past century, banks did not conduct securities or insurance business and could not be affiliated with such firms. That changed in recent years and, with the consolidation of financial sector entities, the number of unaffiliated sources of products and services has declined. For example, a bank may now be affiliated with the broker-dealer through which it once purchased securities for its trust accounts. Trust counsel at one bank that does a lot of municipal bond work told OFIS staff that it's hard for the bank's trust officers to find municipal bonds for trust portfolios that "the bank hasn't touched in some way."

FISCAL/ECONOMIC IMPACT

OFIS has identified the following revenue or budgetary implications in the bill:

(a) To the Office of Financial and Insurance Services: None known

Budgetary:
Revenue:
Comments:

(b) To the Department of Labor and Economic Growth: None

Budgetary:
Revenue:
Comments:

(c) To the State of Michigan: None

Budgetary:
Revenue:
Comments:

(d) To Local Governments within this State: None

Comments:

OTHER STATE DEPARTMENTS

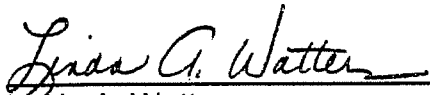
None known.

ANY OTHER PERTINENT INFORMATION

None known.

ADMINISTRATIVE RULES IMPACT

The Office of Financial and Insurance Services has general rulemaking authority under the Code.



Linda A. Watters
Commissioner

9-19-06

Date